



GOVERNOR'S OFFICE OF  
BUDGET AND PROGRAM PLANNING

## Fiscal Note 2017 Biennium

<b>Bill #</b>	SB0407	<b>Title:</b>	Revise tax-exempt status requirements for certain nonprofit pharmacy operations
<b>Primary Sponsor:</b>	Vincent, Chas	<b>Status:</b>	As Introduced

- |   |  |  |
|---|--|--|
| <input type="checkbox"/> Significant Local Gov Impact     | <input checked="" type="checkbox"/> Needs to be included in HB 2 | <input checked="" type="checkbox"/> Technical Concerns   |
| <input type="checkbox"/> Included in the Executive Budget | <input type="checkbox"/> Significant Long-Term Impacts           | <input type="checkbox"/> Dedicated Revenue Form Attached |

### FISCAL SUMMARY

	<b><u>FY 2016 Difference</u></b>	<b><u>FY 2017 Difference</u></b>	<b><u>FY 2018 Difference</u></b>	<b><u>FY 2019 Difference</u></b>
<b>Expenditures:</b>				
General Fund	\$75,571	\$70,142	\$71,299	\$72,478
<b>Revenue:</b>				
General Fund		----- unknown -----		
<b>Net Impact-General Fund Balance:</b>	<u>(\$75,571)</u>	<u>(\$70,142)</u>	<u>(\$71,299)</u>	<u>(\$72,478)</u>

**Description of fiscal impact:** The revenue impact of the bill is unknown. The Department of Revenue will add 1.00 FTE in order to implement this bill at an annual cost to the general fund.

### FISCAL ANALYSIS

#### Assumptions:

#### **Department of Labor and Industry (DLI)**

1. The Board of Pharmacy inspects facilities that participate in the Federal 340B drug discount program, but their participation does not affect the inspection performed, nor does it affect the application for or renewal of their pharmacy license with the state.
2. The board does not involve itself in drug pricing or business relationships unless a compliance issue is reported and involves fraud or billing practices.
3. If a pharmacy involved in the 340B program receives a disciplinary action due to its participation, the board would treat the issue the same as any other compliance issue that might impact a license.

#### **Department of Revenue (DOR)**

4. SB 407 directs the Department of Revenue (DOR) to revoke the tax exempt status of a nonprofit corporation or institution of purely public charity if it engages in a commercial pharmacy enterprise. SB 407 directs DOR to revoke the property tax exemption on any real or personal property or portion of real or personal property used in conducting the commercial pharmacy enterprise. In addition, a fine is to be imposed equal

- to the tax rate of 7% for water's edge corporations times the profit or net pharmacy revenue generated by the commercial pharmacy enterprise, excluding donations, that is derived from sources within the state.
5. The entity subject to the fine shall file its federal exempt organization business income tax return with the department. DOR is to apply all remedies available to the state for the administration, enforcement, and collection of taxes for collection of this fine.
  6. The test of whether a nonprofit corporation or charitable institution is operating a commercial pharmacy enterprise uses six criteria. First, that the nonprofit corporation or institution of purely public charity receives discount drugs pursuant to the federal 340B program. Second, it is in direct competition with a for-profit pharmacy. Third, it claims 340B discounts for most outpatient prescription drugs for privately insured and uninsured patients. Fourth, it sells at least 10% of prescription drugs to privately insured patients at a cost that is less than the cost of purchasing prescription drugs outside the 340B program. Fifth, it sells at least 10% of prescription drugs to privately insured patients at a cost that is more than the cost of purchasing prescription drugs inside the 340B program. The last criterion is that it uses paid staff rather than volunteers.
  7. The federal Public Health Service Act created the 340B program in 1992. It gives certain safety net providers discounts on outpatient drugs comparable to those made available to state Medicaid agencies. Drug manufacturers provide the discounts if they want their drugs covered by Medicaid. To be eligible for the 340B program, entities generally have to either be one of six hospital types or have received one of 10 federal grants. A search of the database maintained by the Health Resources and Services Administration, U.S. Department of Health and Human Services shows 228 eligible entities located throughout Montana (see <http://opanet.hrsa.gov/opa/CESearch.aspx>). However, some institutions had more than one eligible entity. The list appears to include all or most of the hospitals in the state and all or many of the clinics. The list also includes local government entities such county health departments.
  8. DOR is not able to estimate the property tax revenue that would be generated by this bill.
  9. DOR is not able to estimate the revenue that will be generated by the proposed fine in lieu of taxes.
  10. DOR is not able to estimate whether there will be income tax revenue generated by the bill due to provisions of the bill.
  11. SB 407 establishes an entirely new function for DOR, which will require collecting data on prescription drug prices charged by private for-profit pharmacies and 340B qualified entities in locations throughout the state and determining if 340B covered entities should retain their tax exempt status and pay property taxes as provided in the bill.
  12. This fiscal note assumes that the data required for this bill's purposes will need to be collected directly by DOR from private pharmacies and 340B covered entities. If this bill is passed and approved, DOR will seek to use data already available on pharmaceutical use and prices at the state, including at the Department of Labor and Industry and the Department of Public Health and Human Services. However, DOR has not evaluated whether any of that data is suitable to accomplish this bill's purposes and, since any data collected by those departments is intended to support other programs such as worker's compensation or Medicaid, this fiscal note assumes that the data collection will be a new effort.
  13. The department will need to add 1.00 FTE with personal service costs of \$63,438 in FY 2016 and FY 2017, \$64,494 in FY 2018, and \$65,571 in FY 2019.
  14. DOR will have operating costs of \$6,385 in FY 2016, \$6,704 in FY 2017, \$6,805 in FY 2018, and \$6,907 in FY 2019. DOR will incur one-time only costs for equipment and set-up of \$5,748 in FY 2016.
  15. The provisions of SB 407 apply to tax years beginning after December 31, 2015.

	<u>FY 2016 Difference</u>	<u>FY 2017 Difference</u>	<u>FY 2018 Difference</u>	<u>FY 2019 Difference</u>
<b><u>Fiscal Impact:</u></b>				
FTE	1.00	1.00	1.00	1.00
<b><u>Expenditures:</u></b>				
Personal Services	\$63,438	\$63,438	\$64,494	\$65,571
Operating Expenses	\$6,385	\$6,704	\$6,805	\$6,907
Equipment	\$5,748	\$0	\$0	\$0
<b>TOTAL Expenditures</b>	<u>\$75,571</u>	<u>\$70,142</u>	<u>\$71,299</u>	<u>\$72,478</u>
<b><u>Funding of Expenditures:</u></b>				
General Fund (01)	\$75,571	\$70,142	\$71,299	\$72,478
<b>TOTAL Funding of Exp.</b>	<u>\$75,571</u>	<u>\$70,142</u>	<u>\$71,299</u>	<u>\$72,478</u>
<b><u>Revenues:</u></b>				
General Fund (01)	\$0	\$0	\$0	\$0
<b>TOTAL Revenues</b>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>
<b><u>Net Impact to Fund Balance (Revenue minus Funding of Expenditures):</u></b>				
General Fund (01)	(\$75,571)	(\$70,142)	(\$71,299)	(\$72,478)

**Effect on County or Other Local Revenues or Expenditures:**

1. If a nonprofit corporation or charitable institution was required to pay property taxes, local governments would receive a share. However, DOR is not able to estimate the local property tax revenue generated by this bill.

**Technical Notes:**

1. If the intention of the "Commercial pharmacy enterprise" definition is to target transactions in which pharmacies make a profit from selling discounted drugs received in the 340B program, the definition should be clarified.
2. Throughout the bill, the term "privately insured patients" is used. As written, this phrase would appear to exclude Medicare and Medicaid patients. However, the exclusion of Medicare patients seems to be in direct contradiction to the statement of legislative intent found on page 1, line 18-20. If the intention is to include Medicare patients, the term "insured patients" would be more inclusive. Medicaid is already expressly excluded from the term in Section 1(5).
3. Direct competition with a for-profit pharmacy needs to be better defined.
4. In new Section 1 of the bill, (1)(a) appears to be in conflict with (1)(b). Section 1, (1)(a) directs the department to revoke the tax exempt status of the entire nonprofit corporation or charitable institution as defined in 15-6-210, MCA, which addresses tax exempt property, if it engages in a commercial pharmacy enterprise. But (1)(b) directs the department to revoke the property tax exemption on any real or personal property or portion of real or personal property used in conducting the commercial pharmacy enterprise. For purposes of this fiscal note, it is assumed that the property tax exemption applies to the portion of real or personal property used in the commercial pharmacy enterprise, but if this is not a correct interpretation, perhaps this language should be clarified.

5. In new section 1 of the bill, one of the criteria for operating a commercial pharmacy enterprise is that the non-profit or charitable institution is one who claims 340B discounts for most outpatient prescription drugs for privately insured and uninsured patients. “Most” needs to be defined.
6. The long of the revocation period needs to be finds as well as if the revocation can be reversed.
7. SB 407 does not designate where the fines in lieu of taxes are to be deposited.
8. According to a Government Accountability Office (GAO) report on this issue (*Drug Pricing: Manufacturer Discounts in the 340B Program Offer Benefits, but Federal Oversight Needs Improvement*, September 2011, GAO-11-836), for a hospital to qualify for the 340B program, it must be a non-profit. If a Montana hospital or clinic loses its non-profit status at the state level, does that disqualify it from being eligible for the 340B program at the federal level? DOR does not have the expertise to evaluate whether this represents a significant issue or the consequences, if any.
9. SB 407 appears to assume that all 340B covered entities sell prescription drugs directly through in-house facilities. However, the same GAO report referenced above, discusses the fact that many 340B covered entities maintain contracts with private pharmacies instead of maintaining on-premises prescription facilities. The use of contract pharmacies by 340B covered entities in order to provide discounted pharmaceuticals to outpatients is not mentioned in the bill.
10. It is unclear as to how city-county health departments who are 340B covered entities are affected. If they are found to be in violation, does DOR revoke their tax exempt status and assess property taxes? Under 15-6-201(B)(ii) the property and equipment of cities, towns, counties, school districts and the state are exempt from property taxes. This appears to create a conflict between levels of government and different sections of code.
11. Section 2(1) imposes a rate specified in 15-31-121(2), MCA. It appears that 15-31-121(1), MCA, may be intended instead. Additionally, Section 2(1) references net revenue from a commercial pharmacy enterprise. As it is currently written, net revenue appears to capture the profits that a pharmacy made from all sources. If it is meant to capture only net revenue from discounted drugs, the definition should be revised.

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Sponsor's Initials

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Date

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Budget Director's Initials

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Date